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BEFORE THE
SURFACE TRANSPORTATION BOARD
Washington, DC 20423

In the Matter of: **USE OF A MULTI-STAGE DISCOUNTED CASH FLOW MODEL IN DETERMINING THE RAILROAD INDUSTRY'S COST OF CAPITAL**	**STB Ex Parte No. 664 (Sub-No. 1)**

COMMENTS OF ARKANSAS ELECTRIC COOPERATIVE CORPORATION

Pursuant to the Board's decision served February 11, 2008, Arkansas Electric Cooperative Corporation (AECC) respectfully submits the following comments regarding the Board's proposal to use a multi-stage discounted cash flow (DCF) model in conjunction with the capital asset pricing model (CAPM) methodology it has already adopted for calculating the railroad industry's cost of capital AECC and its interests in this proceeding were described in the comments it submitted September 26, 2007 in Ex Parte No 664

In general, AECC defers to the Western Coal Traffic League (WCTL) and other parties to address detailed technical issues regarding CAPM and its implementation by the Board However, in Ex Parte No 664, AECC described how " (t)he Board's proposed computation of carrier-specific 'betas' from railroad stock returns may be affected by considerations other than financial risk that do not arise in most other sectors In the duopolistic operating environment that has evolved for the Class I railroads, anything that has the effect of restricting competition may increase a carrier's stock performance relative to the market, and create the artificial appearance of a 'risk premium' under the contemplated methodology "[1] In response to misleading assertions from the railroads regarding the effect of market power on beta, AECC clarified how, "(b)ecause the exercise of market power in the rail industry does not create a credible prospect of new entry, the Board can reasonably believe that the market power held by the railroads holds down the actual risk they face If the Board observes an increasing beta, it should give careful consideration to the possibility that the higher stock returns driving the beta increase are caused by an increase in the exercise of market power, and not by any increase in the true risk faced by the railroad "[2]

A multi-stage DCF model that doesn't permit the estimated cost of capital to deviate excessively from the long-run growth rate of the economy as a whole appears to provide an element of protection against the potential influence of increased market power on the CAPM methodology In combination with CAPM, such a multi-stage DCF-model could enhance the precision of the resulting cost-of-equity estimate

[1] See AECC's comments submitted September 27, 2007 at page 3
[2] See AECC's written submission dated November 27, 2007 at pages 7-9

AECC appreciates this opportunity to participate in the refinement of the Board's cost-of-capital methodology

Respectfully submitted,

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